

July 2013 Discussion Draft
Proposed Amendments to Mandatory Reporting Regulation
Comments of Morgan Stanley Capital Group Inc.
August 2, 2013

Morgan Stanley Capital Group Inc. (MSCG) appreciates the opportunity to offer these comments in response to the Discussion Draft of proposed amendments to the Mandatory Reporting Rule, published July 17, 2013.

I. Section 95111(a)(4) Imported Electricity from Specified Facilities or Units

MSCG strongly supports what we believe is the underlying intent of the changes to this section, which is to allow parties to sell “specified power” down a custody transfer chain, as long as sufficient documentation exists to demonstrate that the initial purchase was from a Specified Resource or Asset Controlling Supplier, and met all the applicable requirements for being claimed as Specified Power. We do believe, however, that the draft language needs one small tweak to improve precision and avoid an unintended consequence. The language, as currently drafted, appears to require that the initial seller - -i.e. the specified source - - would need to warrant the initial sale as being “specified”. However, the initial seller cannot know this. All the initial seller can warrant is that the initial sale was “unit-specific” or the equivalent (facility-specific or from an ACS). In fact, the only entity that can verify that a power transaction meets all of the conditions for being claimed as “specified” is the one that actually imports the power and is the First Jurisdictional Deliverer. Only that entity can vouch for the fact that the power came from a specified source and was Direct Delivered into California. Other entities in the chain cannot know those facts with enough certainty to provide warranty.

For that reason, we recommend that the proposed new language in the draft, the last sentence in subsection 4, be reconstituted thusly:

Electricity that passes through a chain of custody beginning with a physical generating resource, facility, or Asset Controlling Supplier, and is imported into California by a First Jurisdictional Deliverer, may be claimed as specified under the following conditions:

- A. The entire custody transfer chain is reflected in the relevant E-Tag
- B. The first purchasing entity in the chain warrants that its arrangements with its supplier would meet the resource eligibility criterion of the overall requirements for claiming a specified source (i.e., unit or facility specific, or from an ACS, and obtained pursuant to the “written contract” requirements).
- C. Each subsequent seller in the chain warrants that it has received a qualifying warranty from its supplier

We strongly believe that this language is more technically precise, would be more clearly understood, and requires each entity in the chain to warrant only those things which it can, indeed, know and warrant.

II. Section 95111 (a)(4)(A)(3)

New sentence 3, “Supporting documentation must be provided for busbar claims”, is vague and would benefit from some clarification. First, what might constitute acceptable documentation? Second, does it apply to all busbar claims, or just those referred to in the prior sentence, “2”, regarding claims where the measurement at the busbar is not known?

III. Section 95111 (a)(5)(B)

The new language in 5B is mystifying. It says “Report Asset-Controlling Supplier power that was not properly acquired as specified power as unspecified power”. This language raises several questions. First, it would seem to go without saying that if something is not properly acquired as specified power, it must be reported as unspecified. Under the presumption that the intent is not to belabor the obvious, the question is begged as to exactly what the intent of this language is. Second, other than those not meeting the existing requirements for something to be claimed as specified power, what types of transactions might constitute power being “not properly acquired”? MSCG believes this section adds confusion, not elucidation. If the intent of the language is to say that ACS power bought anonymously on an exchange or through a broker where the source was not known prior to execution of the trade, then the language should just say that instead of making it ambiguous and subject to interpretation. Given that, we may or may not support or oppose the underlying intent.

IV. Section 95111 (a)(5)(D)

Most of the new language in D describes an exception to the treatment of power originating with an ACS, and terms these exceptions “path outs”. MSCG believes this amended treatment is problematic from multiple perspectives. First, it does not appear to be consistent with the way an ACS’s emissions factor is calculated. That factor includes purchases. If, when such purchases are found to be “surplus”, they are sold and assessed an emissions rate other than the ACS weighted average rate, then the calculated ACS rate is no longer accurate, and the total combined emissions rate responsibility will not be equal to the actual GHGs emitted. Second, being able to treat some power as “surplus” begs the question of “over what period?” Minute to minute? Minimum one hour? Average over a day? Something else? Third, there does not appear to be any requirement for an ACS to document that the power it sells is “surplus”, however defined. Fourth, power is always “pooled”. Treatment of some subset of power pool as “system” and some as “surplus” is an arbitrary fiction.

MSCG strongly objects to this proposed new language. As best as we can discern, it is inconsistent with the fundamental intent of the ACS concept. It is our view that an entity that applies for ACS status has voluntarily elected to seek pooled treatment for all of its generation and purchases. In return for this benefit, it forfeits the ability to treat some of its sales as “specified” and some as “unspecified”, or some as “system” and some as “surplus”. Rather, it must calculate a weighted average portfolio value for all of

its sources, both owned generation and purchased power, and any power it sells must be treated as specified and be assessed emissions responsibility at the ACS' weighted average portfolio rate. Allowing an ACS to separate its sales into "system", and "surplus" or "path outs", allows it to "game" the regulatory process to gain a huge competitive advantage. ARB should not allow itself to be manipulated into rule development of this sort, which shifts competitive outcomes in the marketplace without serving a legitimate regulatory purpose.

As a side note, the discussion above induces us to reiterate a previous plea: Somewhere in the regulations, there should be a narrative statement of the underlying concept behind and purpose of the Asset Controlling Supplier program. Debates like the one above are fueled, in part, by different parties making differing assumptions about what the innate principles are that should govern. A prologue describing the innate objectives and goals of things like ACS and RPS Adjustment would prove tremendously helpful in structuring discussions about whether or not implementing details are consistent with the underlying intent. As it is, all participants are left to make their own assumptions, usually inferentially.

V. Section 95111(b)(5)

MSCG finds the language in this new subsection confusing. Is it intended to deal with a hypothetical situation which will never exist in the real world? Presumably, this section is intended to be specific to ACSs, as we are not aware of any provision that lets any other entity type claim a "system power" emission rate. However, no entity that has a system power emission rate above the default emission rate would ever seek ACS status, or any other type of system power rate. If the intent of this section is solely to close such a hypothetical loophole, then we have no concerns. However, the case appears to be so obscure, that we fear it is intended to apply to some other type of situation that is not apparent from the text. If this latter option is indeed the intent, we urge ARB to rethink the draft and make it clearer under what types of situations it might be applicable.

VI. Effective Dates

Finally, MSCG urges ARB to proceed cautiously with regard to any proposed effective dates for new rules. It is hard to make a blanket statement as to whether or not it is appropriate to make changes effective only prospectively or whether it might be appropriate, in some cases, to make changes effective retroactively. We would only caution that in certain cases, making a retroactive change could have huge financial impacts on transactions that took place and were structured under reasonable interpretations of the rules as written at the time.

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